# DEPARTMENT OF STATE REVENUE
# LETTER OF FINDINGS: 00-0287
# Gross Retail Tax
# For the Years 1997 and 1998

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## ISSUE

**I.** **Transactions Subject to Sales Tax** – Sale for Resale or Lease.

**Authority**: IC 6-2.5-2-1; IC 6-2.5-5-8; IC 6-8.1-5-1(d); Monarch Steel v. State Bd. of Tax Comm'rs, 699 N.E.2d 809 (Ind. Tax Ct. 1998); Trinity Episcopal Church v. State Bd. of Tax Comm'rs, 694 N.E.2d 816 (Ind. Tax Ct. 1998); 45 IAC 2.2-8-12(a); 45 IAC 2.2-8-12(b); 45 IAC 2.2-8-12(c); 45 IAC 2.2-8-12(d).

Taxpayer argues that transactions involving the sale of car washing equipment to three of its customers were not subject to the gross retail (sales) tax because those same three customers later resold or leased the equipment.

## STATEMENT OF FACTS

Taxpayer is an S corporation in the business of operating car wash establishments. Taxpayer is also in the business of selling and distributing car washing equipment and supplies to various gas stations and convenience stores. Occasionally, taxpayer will arrange for installation of the equipment at the customer's location.

The Department conducted an audit of taxpayer's financial records and tax returns. The audit determined that taxpayer owed additional sales and use tax. Among other reasons, the audit found taxpayer owed the additional tax because it collected sales tax but failed to remit it to the state and because the audit determined that certain transactions were not exempt.

In addition, the audit noted that taxpayer had either not received, or had not retained, exemption certificates from certain customers. After taxpayer was unable to obtain the missing exemption certificates during the time permitted, the audit assessed additional tax on those particular sales for which no exemption certificate was provided.
Taxpayer submitted a protest of the additional assessment believing it could demonstrate that the source transactions were exempt from sales tax. An administrative hearing was held, and this Letter of Finding follows.

## DISCUSSION

**I. Transactions Subject to Sales Tax** – Sale for Resale or Lease.

Taxpayer agrees that it sold car washing equipment to the three customers but argues that the transactions with each of these particular customers were not subject to sales tax.

Pursuant to IC 6-2.5-2-1, a sales tax is imposed on retail transactions which occur within the state unless a valid exemption is applicable.

IC 6-2.5-5-8 provides a sales tax exemption for transactions involving the sale of tangible personal property acquired by the customer for resale, rental, or leasing. Specifically, the statute reads as follows:

> Transactions involving tangible personal property are exempt from the state gross retail tax if the person acquiring the property acquires it for resale, rental or leasing in the ordinary course of his business without changing the form of the property.

Typically, a purchaser of personal property exempt under IC 6-2.5-5-8 issues an "exemption certificate" to establish that the personal property being acquired will be used in an exempt manner. 45 IAC 2.2-8-12(a) reads in part that, "Retail merchants, manufacturers, wholesalers and others who must register with the Department of Revenue and who qualify to purchase exempt from tax under this Act may issue exemption certificates with respect to exempt transactions."

Because the taxpayer was engaging in retail transactions by selling its car washing equipment and supplies, its initial obligation was to collect the sales tax. 45 IAC 2.2-8-12(b) states, "Retail merchants are required to collect the sales and use tax on each sale which constitutes a retail transaction unless the merchant can establish that the item purchased will be used by the purchaser for an exempt purpose."

The Department presumes that every intra-state sale of tangible of personal property is subject to sales tax; it is the buyer's and the seller's obligation to establish that the particular transaction is exempt. The simplest way to meet this burden is for the buyer to issue an exemption certificate. 45 IAC 2.2-8-12(c) provides that, "All retail sales of tangible personal property for delivery in the state of Indian shall be presumed to be subject to sales or use tax until the contrary is established. The burden of proof is on the buyer and also on the seller unless the seller received an exemption certificate."
Because the taxpayer was unable to supply copies of the missing exemption certificates, the audit correctly assumed that the transactions with the three customers were subject to the gross retail tax. However, taxpayer now asserts that it can demonstrate the sales to the three customers were exempt. 45 IAC 2.2-8-12(d) provides the taxpayer two alternative means of doing so. "Unless the seller receives a properly completed exemption certificate the merchant must prove that sales tax was collected and remitted to the state or that the purchaser actually used the item for an exempt purpose."

Because the audit determined the transactions with the three customers were not exempt, the taxpayer now has "[t]he burden of proving that the proposed assessment is wrong." IC 6-8.1-5-1(d). In determining whether a taxpayer is entitled to an exemption, such as that provided for in IC 6-2.5-5-8, the courts have held that the exemption is to be strictly construed against the taxpayer and in favor of taxation. Monarch Steel v. State Bd. of Tax Comm'rs, 699 N.E.2d 809, 811 (Ind. Tax Ct. 1998); Trinity Episcopal Church v. State Bd. of Tax Comm'rs, 694 N.E.2d 816, 818 (Ind. Tax Ct. 1998).

Because the circumstances surrounding the sales to the three customers vary and because taxpayer's efforts to demonstrate the various transactions with the three customers also vary, the transactions with three customers are addressed individually.

**A. Customer One**:

In the case of Customer One, taxpayer has been able to provide a copy of an exemption certificate. The exemption certificate was signed on January 12, 2000, was prepared by Customer One's vice-president, and states that "all purchases of tangible personal property from [taxpayer] dating from 3/31/98 to 3/31/98 by the undersigned on which sales or use tax was not paid at time of purchase were used for a purpose which is exempt under provisions of the Indiana Gross Retail Tax Act." Therefore, in regard to Customer One, taxpayer has plainly met its burden of demonstrating that it was not required to collect sales tax on the sales of tangible personal property to Taxpayer One which occurred on "3/31/98."

**B. Customer Two:**

According to taxpayer, Customer Two is a financing agent. Although taxpayer negotiates with the end-user of the car washing equipment – such as a gas station or a convenience store – the typical end-user has neither the means nor the inclination to purchase the equipment directly from taxpayer. Instead, once the end-user expresses an interest in obtaining the equipment, taxpayer introduces the prospective end-user to a financing agent, such as Customer Two, which can provide the necessary financing. Thereafter, taxpayer sells the equipment to the financing agent, the financing agent pays taxpayer the total cost of the equipment, the equipment is delivered directly to the end-user, and the end-user makes successive payments to the financing agent.

Taxpayer argues that its sales to Customer Two – now no longer in business – were exempt from sales tax because Customer Two was in the business of leasing the equipment to the end-user. Taxpayer relies on IC 6-2.5-5-8, which exempts sales "if the person acquiring the property acquires it for resale, rental, or *leasing in the ordinary course of his business . . . .*" (*Emphasis added*). Taxpayer was not able to obtain an exemption certificate from Customer Two. Instead, taxpayer has provided a copy of an invoice taxpayer sent Customer Two. The invoice lists Customer Two's out-of-state address and indicates that the equipment is to be delivered to a third-party – presumably the end-user – located at an in-state address. In addition, the invoice states that, "Any applicable taxes are responsibility of [Customer Two]." Presumably, this last statement is a stipulation between the two contracting parties requiring Customer Two to collect sales tax from the individual end-user.

Insofar as the sales transactions with Customer Two, taxpayer has failed to "prove that sales tax was collected and remitted to the state or that the purchaser [Customer Two] actually used the item for an exempt purpose." 45 IAC 2.2-8-12(d). Standing alone, the invoice sent Customer Two is insufficient to establish Customer Two purchased the car wash equipment for an exempt purpose or that the gross retail tax was ever paid to the state.

**C. Customer Three:**

Taxpayer indicates that Customer Three was also a financing agent. As a result, taxpayer maintains its sales of equipment to Customer Three were exempt from sales tax under IC 6-2.5-5-8 because Customer Three acquired the equipment in order to lease it to third-party end-users. Because taxpayer has not submitted a copy of the relevant exemption certificates, the transactions are presumably subject to sales tax, and taxpayer has the burden of proving that the transactions were exempt. IC 6-8.1-5-1(d); 45 IAC 2.2-8-12(c).

As in the case with Customer Two, taxpayer has submitted a copy of an invoice it sent to Customer Three indicating Customer Three was located at an out-of-state location and that the equipment was delivered to a third-party which had a different, in-state address. In addition, taxpayer has submitted a copy of what purports to be Taxpayer Three's standard lease agreement form. The lease agreement form states that the "[Third-Party Lessee] shall pay all charges and taxes (local, state, and federal) which now be imposed upon the ownership, leasing, rental, sale, purchase possession, or use of the Equipment . . . ."

In further support of its argument, taxpayer has provided a copy of a letter dated December 1997 and received from Customer Three. In that letter, Customer Three indicates that the Named End-User has "entered into a lease agreement with [Named End-User] covering equipment purchased from your firm." The letter also requests taxpayer to, "[p]lease be sure no tax appears on the invoice."

Insofar as its transactions with Customer Three, taxpayer has met its burden of proving that Customer Three purchased the car wash equipment – which it subsequently transferred to the Named End-User indicated in the December 1997 letter – "for an exempt purpose." 45 IAC 2.2-8-12(d). Accordingly, taxpayer is entitled to the sales tax exemption set out in IC 6-2.5-5-8 for the sale of equipment made to Customer Three and which was subsequently leased to the Named End-User.

## FINDING

Taxpayer's protest is sustained in part and respectfully denied in part. Taxpayer is entitled to the exemption on sales made to Customer One on "3/31/98." Taxpayer is not entitled to an exemption on sales made to Customer Two. Taxpayer is entitled to the exemption on sales of equipment made to Customer Three and thereafter leased to the Named End-User identified in the December 1997 letter.